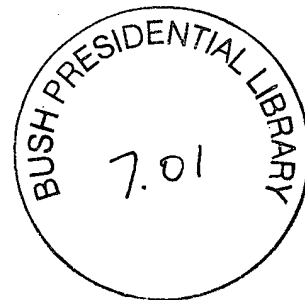


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Directorate of Intelligence  
Office of Slavic and Eurasian Analysis

No. 22

## NIS Reform Developments

27 November-9 December 1992

*Economic reform in Russia suffered a serious setback, at least in the short run, as the Congress of People's Deputies voted against confirming Gaydar as Prime Minister, sent the government's economic program back for reworking and failed to renew Yel'tsin's special economic powers. The government has pledged to soldier on, but reform and the economy are now hostage to the resolution of Yel'tsin's confrontation with the Congress.*

### RUSSIAN DEVELOPMENTS

**Yel'tsin forces Showdown.** Yel'tsin has responded to the Congress' refusal to confirm Gaydar as Prime Minister, its enactment of a resolution directing substantial changes to government economic policy and its failure to renew Yel'tsin's decree-making powers with a call for a January referendum to determine whether the President or the Congress will lead the country--especially with regard to the economy. The unfolding constitutional

crisis will hamstring the government's efforts to stabilize and reform the economy. Yel'tsin's earlier decree appointing Gaydar Acting Prime Minister will remain in force for the time being. Meanwhile, the government will try to respond to the economic resolution that gives it one month to present a revised economic plan for Supreme Soviet approval and that calls for the incorporation of potentially damaging measures (see box).

Questions, comments, or suggestions for items to be covered in future issues may be directed to Chief, Economic Performance Division, on

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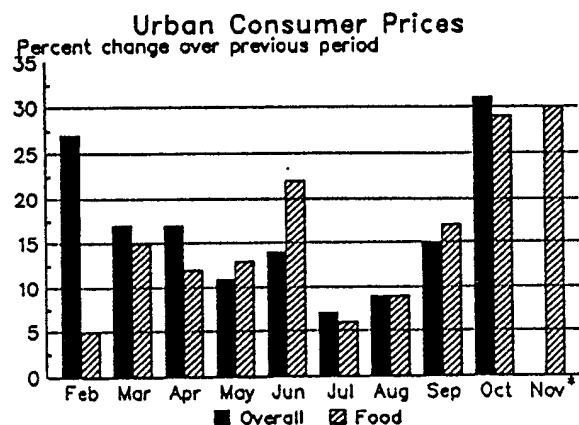
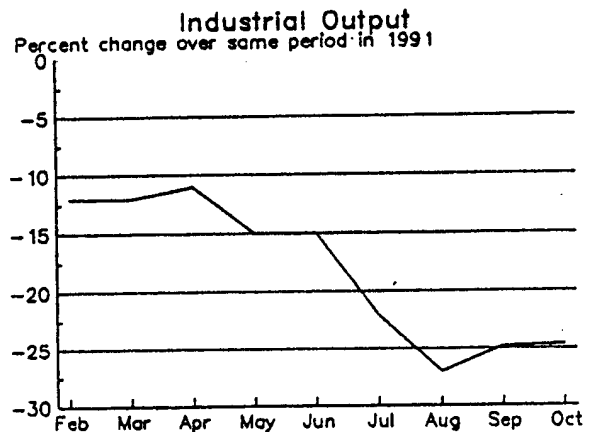
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The Congress' economic resolution calls for:

- o Resolution of social problems and the development of legislation to ensure a minimum standard of living as key preconditions for reform.
- o Subordination of financial and credit policy to the development of priority sectors and tempering the production decline.
- o Replenishment of enterprise working capital.
- o State regulation of investment, prices, credit, and monopolies.
- o Rebuilding of CIS economic ties.
- o Prevention of the breakup of "unified technological complexes" by privatization.
- o Creation by March 1993 of a foreign trade strategy that regulates the exchange rate, secures critical imports, and establishes parliamentary control over the acceptance, use, and repayment of foreign credits.
- o Indexation of agricultural product prices apparently to compensate for the rise in input prices.

and preliminary figures suggest that this was also the case in November. In some sectors, such as ferrous and nonferrous metals, machine building, and light industry, daily output in October and November reportedly exceeded average levels recorded in the third quarter. Inflation, meanwhile, accelerated as urban consumer prices rose by an estimated 30 percent in October and probably by a similar amount in November, driven primarily by food price increases. In his speech to the Congress, Gaydar indicated that the government began tightening its budgetary policy in September to slow inflation.



\*Russian Government forecast.

## Prices and Supplies

**Economic Decline Pauses but Inflation Accelerates.** According to Russian government statistics, the rate of decline in industrial production stabilized in October,

## Privatization and Demonopolization

### Market Price of Vouchers Increases.

According to *Izvestiya*, the price of vouchers sold on the Russian Commodities and Raw Materials Exchange rose sharply during the last week of November, increasing from an average of 4,100 rubles to 7,500 (their face value is 10,000 rubles). The jump in market price followed an announcement by the State Property Committee that several large voucher auctions will be held in Moscow, St. Petersburg, Vladimir and Yaroslavl' beginning on 9 December. A number of large industrial enterprises, tourist hotels, and *beryoza* shops are scheduled to be sold. The well-known and reportedly very profitable Bolshevik Cake Factory will be the first firm put up for sale in Moscow. In a move to help voucher holders decide where to invest their privatization checks, the government also announced it is setting up an information center, called the Russian Agency for International Cooperation and Development, that will maintain data bases on the production, profitability, and incomes of all Russian enterprises.

**New Decrees Support Private Enterprises.** Last week President Yel'tsin signed two decrees designed to strengthen the financial position of private enterprises. One decree, long advocated by Property Committee Chief Chubays, prohibits discrimination against privately owned enterprises in the granting of government credits, while the other provides special tax breaks, insurance against loss, and guarantees for foreign investors. To help promote private business interests, a conference of leaders of joint-stock companies announced the formation of a new Association of Private and Privatized Russian Enterprises.

**Money Talks at City Kiosks.** Big city consumers are witnessing the mushrooming of kiosks where money buys almost any consumer good but often at high prices. These movable shops--the latest have plexiglass fronts and accommodate as many as 10 customers inside--line the main streets of Moscow, St. Petersburg, and other cities. The kiosks sell a wide variety of goods, including candy, clothes, liquor, shoes, and videos, and many accept rubles as well as hard currency. A few kiosks even sell privatization vouchers, according to Property Committee Chief Chubays. Once criticized for offering only foreign goods, many kiosks now sell Russian products. For example, the availability of food blenders surprised some customers who did not even know that Russia produced them. In what is becoming a trend, one Moscow meatpacking plant has cut off deliveries to its traditional customers--state-owned stores--and now earns more by sending its products directly to a kiosk. Competition from the kiosks is encouraging many state stores to spruce up their facilities and to rent out space to private businesses as a way of adding stock and drawing customers.

**Private Farms Increase.** Russian farmers continue to establish peasant farms--family operated farms of less than 100 hectares--at a rapid rate. As of 1 October, there were 148,700 peasant farms, compared with the government's 1992 goal of 150,000. Meanwhile, Yel'tsin's decree of nearly a year ago ordering state and collective farms to choose among several organizational options by the end of this year seems to have bogged down, with fewer than half of the farms registering as ordered. Moreover, nearly half of those that have registered have opted to keep their former state or collective designation. Most of the rest are choosing to be reorganized into joint stock companies. The decree also called for shutting down unprofitable state

and collective farms, but there have been no reports of this yet.

**Vouchers to be Issued for Land.** Russian privatization czar Chubays announced on 7 December that the Russian government will soon propose a plan to issue all citizens vouchers for the purchase of small plots of land. This follows the constitutional amendment on land approved Saturday by the Congress of People's Deputies that permits the sale of small plots as long as a buyer agrees to use the land for gardening or house building. Neither the amendment nor the voucher program applies to peasant farms, which are the fastest-growing area of private agricultural activity. The land vouchers would differ from the privatization vouchers now being distributed in that they could be used only for land and could not be traded freely. Chubays said the government will submit the specifics to the Supreme Soviet early next year.

**Moonlighting Increases.** A growing number of Russian workers are taking second jobs to supplement falling real incomes. A survey conducted by a local business journal found that about one-third of the state labor force in Irkutsk--a city of 650,000 inhabitants located in East Siberia--is moonlighting in the private sector. The respondents said they preferred to earn extra money by working in agriculture (18 percent), construction (16), middleman services (12), creating intellectual products (10), trading (8), metalworking (6), and woodworking (5). Irkutsk has been cited in the Russian business press as a leader in privatization, and, according to recent Embassy reporting, 50 to 60 percent of its retail trade and consumer service establishments are in the process of being privatized.

## Foreign Economic Relations

**Domestic Bankers Seek to Restrict Foreign Banks.** Russia's domestic banking industry is putting pressure on the government to restrict foreign bank activity in response to efforts by several foreign banks to open full-service branches in Moscow and St. Petersburg. Last month a draft resolution was considered by Parliament that would require the Central Bank to stop issuing operating licenses to foreign banks until 1 January 1994 and to suspend licenses already granted until that date. Supporters of the resolution attempt to justify it as a way of stemming capital flight, but their real intent is to limit foreign competition. However, because of opposition to the measure from some legislators, a final vote on it was postponed indefinitely. In order to get around this postponement, the Central Bank is planning to implement new regulations on foreign banks that would prohibit them from taking deposits from non-bank Russian sources. Loan activities would remain unconstrained, however.

**Russia Limits Oil Exports to Former Soviet Republics.** Government officials have announced that Russia will export only 50-55 million tons of oil next year to former Soviet republics, down from 70-75 million tons this year and 100 million tons in 1991. Russia will guarantee delivery of half of the 50-55 million tons in return for imports critically needed by Russian enterprises. The terms of these state-to-state barter deals have not been determined, but the effective price of oil will probably be close to world levels. Moscow's new industrial supply organization, Rosskontrakt, has been tasked to ensure that quarterly exports of oil under state guarantees are balanced by the agreed-upon flows of imports. To obtain the other half of the promised 50-55 million tons of oil, former republics will have to negotiate

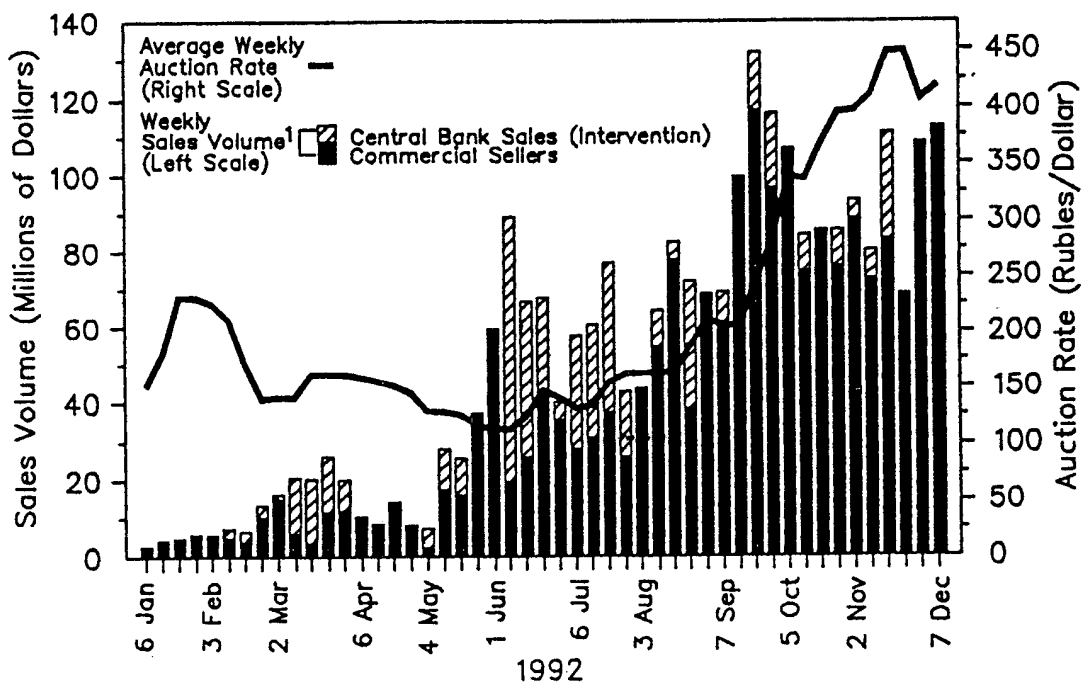
directly with Russian oil enterprises, which will probably demand world market prices and, in some cases, payment in hard currency. Russia will not guarantee gas deliveries, but expects gas deliveries to remain at current levels.

### Ruble Rises in Strength, Then Falls.

Last week the ruble posted its first significant gains since early October, rallying from 447 rubles per dollar at the start of Tuesday's auction on the Moscow Interbank Currency Exchange to 398 rubles at the closing bell on Thursday (see figure). Central Bank officials attributed the rise to enterprises' need for rubles to settle end-of-year accounts, reduction of the inflow of rubles calming of investor fears over the current from other republics, and a

temporary legislative Congress. The bank used the opportunity to build up its hard currency reserves by buying more than \$30 million, its first large-scale purchases of hard currency on the exchange. Central Bank intervention may also have been intended to smooth the ruble's rise. Market analysts estimate that the ruble could have strengthened to as much as 350 rubles per dollar had the bank not purchased dollars. It is unlikely, however, that this most recent rally signals a market bottom. Inflation--the driving force behind the ruble's long slide--remains stubbornly high. On Tuesday (8 December) the ruble resumed its fall, weakening to 419 rubles per dollar.

## Trading on the Moscow Interbank Currency Exchange



<sup>1</sup>Total weekly-sales volume is known. Central Bank intervention can only be estimated, and is probably significantly greater than shown here.

## DEVELOPMENTS IN OTHER NIS STATES

**Ukraine Unveils Privatization Program.**  
Kiev announced plans to open privatization bank accounts for all Ukrainian citizens that can be used only for purchasing shares in state-owned shops and firms. The accounts will amount to 30,000 coupons--roughly equivalent to four months' wages--and will not be transferable. The plan envisions using public auctions to privatize 25 percent of small state businesses within four months. Prime Minister Kuchma has been a vocal supporter of small scale privatization and this plan probably reflects strong backing from him. Hardline opposition in the cabinet and Ukraine's inadequate legal and institutional infrastructure, however, will likely slow progress on implementation.

**Estonian Banks Declare Moratorium.**  
The Bank of Estonia in mid-November seized control over two of the country's largest commercial banks, Tartu Commercial Bank and Union Baltic Bank, and placed restrictions on withdrawals from a third bank. The affected banks hold about half the bank accounts in Estonia. According to Prime Minister Laar, the move was a preemptive effort to prevent their imminent bankruptcies. Bank officials believe that the Union Baltic Bank may be salvageable but anticipate that the Tartu Commercial Bank will eventually be closed down. These commercial banks, like many in the former USSR, are woefully undercapitalized and have large portfolios of nonperforming loans. The banks were also hurt by the freeze on hard currency accounts held in Vneshekonombank in Moscow.

## SPECIAL ANALYSIS

### New Russian Investment Policy: Deja Vu?

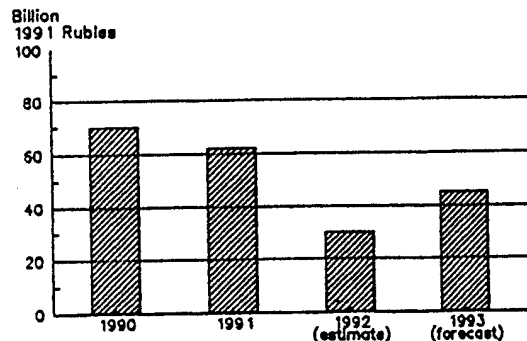
*After sharply cutting state-funded investment this year, the Russian government plans to increase it by nearly half in real terms in 1993. The decision reflects the government's effort to meet the needs of investment-starved sectors such as energy, food processing, and transportation, to support defense conversion, and to quiet major industrial lobbyists such as Civic Union. The government also plans to take measures designed to stimulate alternative sources of investment funding, such as tax breaks and bank credits for enterprises that invest. If targeted effectively, increased investment from the budget could help slow the decline in output. But the dangers are that political rather than economic considerations will determine the allocation of investment, enterprises will continue to rely on state support, and the policy could be highly inflationary.*

### Unfulfilled Expectations

In an effort to reduce Russia's budget deficit, the government slashed budget-funded investment this year by at least 50 percent in real terms from last year's level. Major sectors including construction, energy, and agroindustry were the most affected. The cuts were particularly sharp in September as the government sought to slow inflation. The government had hoped that other sources of investment--mainly enterprise funds--would help offset the cut in state funding. But by mid-summer, Acting Premier Gaydar, who had harshly condemned the old system of centrally directed investment as economics editor of *Kommunist*, was forced to acknowledge that alternative investment sources had failed to live up to

expectations. Many enterprises were financially strapped and had little money to spend on capital improvements or repair. Gaydar also noted that private savings were insufficient, investment institutions poorly developed, and foreign investment low because of the country's political and economic uncertainties.

Russia: State Budget Investment 1990-1993



Source: Derived from Russian official figures.

The government has increasingly come under fire from industrial interest groups such as Civic Union because of the low level of investment. Civic Union stated in October that it is "altogether impermissible" to sacrifice investment to "the dogma of a deficit-free budget" and called for an expansion of government investment and credits to maintain production and prevent large-scale unemployment.

### Seeking To Boost Investment

In response to growing concerns over the industrial decline and the crumbling infrastructure, and mounting criticism from industrial interests, the government's draft 1993 budget calls for investment spending to increase by about half in real terms--an increase of about 2 to 3 percentage points of budget expenditures. In a recent speech to the Supreme Soviet, Gaydar indicated that high priority will be given to transportation, fuels and energy, specific projects in metallurgy, chemicals, and